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Financial Markets

Irving Trust

Irving Trust Company
One Wall Street
New York, NY 10015

Economic Research & Planning Division

Friday
(Noon)

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Yesterday, M1 dropped sharply to the bottom of its target range. Last month, M1's growth rate from its fourth-quarter 1983 base averaged only about 5% at an annual rate. Despite a great deal of good news recently, the bond market has been unable to improve. Indeed with M1 growth exceptionally weak, and M2 and M3 within their targets, the bond market has continued to give up ground. While this is not too surprising a result shortly before a new Treasury refunding, it has now been going on for about a month. There is something to be learned from the market's inability to improve on what should be good news.

There clearly is concern about who will buy the securities the Treasury is scheduled to offer next week. Nominally they will be purchased by the government securities dealers, but the dealers are concerned about who they can distribute these to and at what price. The failure of securities to change hands after yesterday's excellent money number--as large a decline as almost anyone dared to forecast--indicated how reluctant the professional community is to increase holdings of securities at this time. If retail investors have any interest in buying long-term paper, there is no indication that they have begun to satisfy these demands. But it is auction time, and all the participants are playing their cards close to the vest.

The market may have been unnerved recently by the relatively high level of the Fed funds rate. For each of the first seven days of the current CRA period, funds have traded at a higher level than for any of the corresponding days of any previous CRA period. However, at its press conference on Thursday, the Fed "explained away" the high Fed funds rate of early this week by saying that an expected drawdown in Treasury balances had failed to materialize. Therefore, the market was left less liquid than the Fed had intended. The three-day RPs the Fed executed on Monday (April 30) probably didn't put the market in the position the Fed had hoped for. These RPs were not renewed Thursday because Social Security payments and net Treasury bill redemptions from the Monday bill auction will be supplying reserves. There is good reason to believe that, in addition to these Fed operations, large transfers of funds involving the financial settlement of a large merger were distorting the funds rate.

Also remember that the market is forward looking. Over the long haul, the markets remain wary of large Federal budget deficits. Near term, this becomes a fear of strong credit demand in general. Over the coming weeks, loan demand is expected to be strong, affected in part by merger-related borrowing. M1 should increase next week, but the expected rise of $2-3 billion is not really a factor, given where M1 lies in its target range. M2 and M3 will also be released next week: M2 should register moderate growth; M3 might be a bit of a problem. Even so, the news on the horizon isn't really that bad. Right now, the worst problem is the market's gloomy psychology.

Robert A. Brusca

Irving Trust

Market Yields

	5/4/84 (Noon)	Week Ago	Year Ago
Prime Lending Rate at Irving Trust Company	12.00%	12.00%	10.50%
Effective since	4/5/84		
Discount Rate at Federal Reserve Bank	9.00	9.00	8.50
Federal Funds	10.00	10.43	8.38
Repurchase Agreements	9.50	9.50	8.38
U.S. Treasury Issues			
Bills			
3 months	10.20	9.92	8.30
6 months	10.80	10.43	8.43
1 year	11.22	10.98	8.59
Coupons			
2 years	12.02	11.86	9.23
4 years	12.53	12.35	9.63
7 years	12.87	12.68	10.08
10 years	12.95	12.75	10.16
Long Bond	12.98	12.80	10.30
Negotiable Certificates of Deposit-Secondary Market			
1 month	10.50	10.25	8.30
3 months	10.65	10.50	8.35
6 months	11.00	10.85	8.30
1 year	11.50	11.50	8.70
Banker's Acceptances			
1 month	10.41	10.25	8.31
3 months	10.68	10.50	8.33
6 months	11.10	10.90	8.39
Eurodollar Deposits			
1 month	10.75	10.68	8.69
2 months	11.00	10.87	8.75
3 months	11.18	11.00	8.75
Commercial Paper - Prime Names			
Directly placed by:			
Finance Companies			
1 week	9.87	10.16	8.51
1 month	10.34	10.43	8.42
3 months	10.41	10.51	8.41
Bank Holding Companies			
1 month	9.83	9.84	8.17
Dealer Placed:			
3 months	10.62	10.72	8.44
New AA Corporate Utility Bond	14.30	14.00	11.30
Tax Exempt			
6 month Project Notes	5.65	5.65	4.70
1 year AAA Bond	5.75	6.00	5.00
5 year AAA Bond	7.40	7.45	6.30
20 year AAA Bond	9.75	9.50	8.30

This information represents prevailing market yields.
It should not be construed as an offering.
All yields are on the offered side of the market.

Cable Address:
"IrvingBank" Telex: I.T.T. 420268 • R.C.A. 232241
W.U.I. 62832 • French 82629